Internal Revenue Service

memorandum

CC:TL-N-5863-91
Br3:WEMcLeod

date: July 1991

to: District Counsel, Philadelphia MA:PHI

from: Assistant Chief Counsel (Tax Litigation) CC:TL

subject: [redacted]

This is in response to your request for tax litigation advice regarding what effect the Railroad Retirement Board's (RRB) decision, that [redacted] ([redacted]) is not an employer under the Railroad Retirement Act (RRA), has on the Service's determination that [redacted] is an employer under the Railroad Retirement Tax Act (RRTA).

Issues:

1. Whether the Service is bound by the decision reached by the RRB that [redacted] is not a covered employer under the RRA.

2. Whether the doctrines of res judicata or collateral estoppel apply to decisions of a federal agency such as the RRB in light of decisions such as Scammerhorn v. Railroad Retirement Bd. of United States, 748 F.2d 1008 (5th Cir. 1984), and Castillo v. Railroad Retirement Bd. of United States, 725 F.2d 1012 (5th Cir. 1984).

3. Assuming the Service is not bound by the decision of the RRB, whether there is a procedure for resolving disputes between the two agencies.

Summary:

1. It is the Service's long standing policy that it is not bound by any decision rendered by the RRB because I.R.C. § 7801(a) vests the authority to administer and enforce the Internal Revenue Code solely with the Secretary of the Treasury.

2. Because the decisions made by the Service and the RRB are with respect to different statutes, res judicata does not apply here. While an argument can be made that collateral estoppel applies, it is the Service's position that the doctrine is not applicable because the issues in the two proceedings are not identical, there is no privity between the RRB and the Service due to different statutes being involved, and there was no final decision by the RRB from the government's perspective

since only private claimants have the right to appeal the RRB's decisions.

3. The procedure for resolving disputes between the two agencies is set forth in CCDM (39)636.22. If further resolution is required, the dispute may be presented to the Attorney General of the United States. However, a referral to the Attorney General is generally reserved for instances where litigation between the two agencies might result from the dispute. The dispute over [redacted] coverage under the railroad retirement system will not result in such litigation. Moreover, the Service is planning to contact the RRB again hopefully to resolve this matter.

Facts:

[redacted] (Leasing), and [redacted] are wholly owned subsidiaries of [redacted] (Industries). Industries also owns rail carrier subsidiaries which were acquired in [redacted] ([redacted]), and [redacted], [redacted] ([redacted]). [redacted] ceased operations in [redacted]. Industries was formed in [redacted] and adopted its present name in [redacted]. It had no employees as of [redacted]. It appears to own railroad locomotives which it leases to [redacted].

Industries conducts its freight car leasing business through Leasing. Leasing is in the business of arranging financial transactions for and leasing freight cars primarily to unaffiliated companies and railroads. Only a minor number of cars are used by one of its affiliated railroads for its railroad freight hauling business.

[redacted], which was formed in [redacted], is in the business of rebuilding, assembling, and repairing freight cars for unaffiliated companies and for Industries. [redacted] performs its repair car functions primarily for Industries' leased fleet and for unaffiliated companies, with only [redacted] percent of its work being done on railcars used by [redacted] in its freight hauling operations. One of Industries' rail carrier subsidiaries furnishes [redacted] with connecting service to other railroads. The railcars enter and leave [redacted]' facility on the [redacted]'s tracks, with motive power supplied by [redacted].

[redacted], which was formed in [redacted], performs virtually all of its repair functions for Industries' leased fleet and unaffiliated companies. Leasing, [redacted], and [redacted] do not own or operate any railcars.

Industries' directors or principal officers are also directors or principal officers of its rail carrier subsidiaries. [redacted] percent of Industries' customers are railroads.

In late [redacted], the RRB requested information from Industries concerning its ownership of [redacted] and [redacted]. Industries responded in [redacted]. By letter dated [redacted], Industries was notified that the RRB's General Counsel had determined, in Opinion No. [redacted], that Industries was a covered employer under RRA and RUIA, effective as of [redacted], when Industries acquired [redacted]. Industries requested reconsideration of the initial decision and provided additional information. By letter dated [redacted], the General Counsel for the RRB determined that Industries was not a covered employer but determined that Leasing, [redacted] and [redacted] were covered employers. This decision was appealed to the RRB in [redacted]. On [redacted], the RRB, in a two to one vote, reversed the General Counsel decision.

In [redacted], the RRB also provided information to the Service that [redacted] was a covered employer under the RRA and RUIA. Subsequently, the Service began an examination of [redacted]. By letter dated [redacted], Industries advised the Service as to the status of its subsidiaries' appeals pending before the RRB. Subsequently, the Service received the RRB's decision of [redacted]. By letter dated [redacted], the revenue agent advised [redacted] that she was requesting technical advice because she found no persuasive arguments which permitted the reversal of the decision of the General Counsel of the RRB. The technical advice request involved tax years [redacted] through [redacted]. The subsidiaries submitted a [redacted] page memorandum in response to the request for technical advice arguing that (1) the doctrine of res judicata bars the Service from proceeding against the subsidiaries; (2) the subsidiaries are not under common control with Industries and do not perform any service in connection with transportation by railroad. On September 12, 1986, the Service issued its technical advice memorandum holding that the subsidiaries were under common control with Industries and that the subsidiaries each performed services vital to the transportation services of many rail carriers. The memorandum did not address the issue of res judicata. By letter dated [redacted], the Service proposed RRTA tax assessments against [redacted] for [redacted] through [redacted] in the amount of $[redacted], plus interest. [redacted] submitted a letter of protest dated [redacted], and requested a conference with Appeals.

Discussion:

Issue 1:

The RRTA and RURT are part of the Internal Revenue Code. I.R.C. § 7801(a) vests the authority to administer and enforce the Internal Revenue Code with the Secretary of the Treasury. The RRA and RUIA are part of Title 45 of the United States Code. Both Acts provide that they will be administered by the RRB.

There is nothing in the Internal Revenue Code, the RRA, nor RUIA which gives the RRB any power to enforce or administer the Internal Revenue Code.

It is our position that, for purposes of RRTA and RURT, the Service determines whether a taxpayer is a rail employer independent of any determinations made by the RRB with respect to the RRA and RUIA. The RRB shares this view. We have won and lost cases where the determination was made by the Service. In any case, either no reference was made to any determinations made by the RRB or the RRB's determination conflicted with the Service's determination. For example, Atlantic Land & Imp. Co. v. United States, 790 F.2d 853 11th Cir. 1986) (here we won); Standard Office Building Corporation v. United States, 819 F.2d 1371 (7th Cir. 1987) (here we lost). A contrary position would invalidate revenue rulings where we determined whether a taxpayer was a rail employer independent of any determination by the RRB. See Rev. Rul. 74-552, 1974-2 C.B. 338; Rev. Rul. 77-386, 1977-2 C.B. 356; Rev. Rul. 77-445, 1977-2 C.B. 357. A contrary position would also require us to revisit and revise GCMs and the IRM regarding our relationship and coordination procedures with the RRB. See GCM 37091, I-28-77 (April 18, 1977); GCM 37114, I-496-76 (May 10, 1977); GCM 38078, I-8-78 (September 5, 1979); CCDM (39)636.22.

Issue 2:

The second issue for which you requested advice was whether the doctrines of res judicata or collateral estoppel applied to the RRB decision that [redacted] was not a covered employer so as to preclude the Service for maintaining that [redacted] was a covered employer under the RRTA. While there are serious litigating hazards involved, we believe that the Service could make a defensible argument that collateral estoppel should not apply in this circumstance.

The doctrine of res judicata is judicial in origin and is intended to prevent repetitious lawsuits involving the same cause of action thus promoting repose of past disputes. The doctrine rests upon considerations of economy of judicial time and public policy favoring the establishment of certainty in legal relations. Commissioner v. Sunnen, 333 U.S. 591, 597 (1948). In Sunnen, the Supreme Court explained the doctrine of res judicata as follows:

> The rule provides that when a court of competent jurisdiction has entered a final judgment on the merits of a cause of action, the parties to the suit and their privies are thereafter bound "not only as to every matter which was offered and received to sustain or defeat the claim or demand, but as to any other admissible matter which might have been offered for

> that purpose." Cromwell v. County of Sac, 94 U.S. 351, 352[(1876)]. The judgment puts an end to the cause of action, which cannot again be brought into litigation between the parties upon any ground whatever, absent fraud or some other factor invalidating the judgment. [333 U.S. at 597. Citations omitted.]

Res judicata thus "preclude[s] parties from contesting matters that they have had a full or fair opportunity to litigate [and] protects their adversaries from the expense and vexation attending multiple lawsuits, conserves judicial resources, and fosters reliance on judicial action by minimizing the possibility of inconsistent decisions." Montana v. United States, 440 U.S. 147, 153-154 (1979).

Three requirements are contained in Sunnen's definition of res judicata: first, the parties in the subsequent litigation are the same or in privity with the parties in the original litigation; second, the cause of action is the same; and third, there was a final decision of the merits in the first action. 333 U.S. at 597. Res judicata clearly does not apply in this case because the causes of action are different. In a tax case, a tax liability for a single year is a single cause of action. Id. at 598. However, the controversy involving [redacted] consists of two separate causes of action. The first, decided by the RRB, involved whether [redacted] was a covered employer under the RRA. The Service, on the other hand, is examining whether [redacted] is a covered employer under the similar, but distinct, RRTA. Although [redacted]'s protest refers to res judicata, the critical issue is whether collateral estoppel applies in this case. Collateral estoppel is a subdivision of, and more narrowly focused than, res judicata.

The doctrine of collateral estoppel declares that once a court has decided an issue of fact or law necessary to its judgment, that decision is conclusive in a subsequent suit based on a different cause of action to bind a party to the prior litigation. Restatement (Second) of Judgments § 27 (1982). The Tax Court has stated the requirements necessary for collateral estoppel to apply in a case. First, the issue in the second case must be identical to the one decided in the first case. Second, there must be a final judgment by a court of competent jurisdiction. Third, the parties to the second suit must be the same or in privity with the ones in the first suit. Fourth, the parties must have actually litigated the issue and its resolution must have been essential to the prior decision. Finally, the controlling facts and applicable legal rules must remain unchanged from those in the prior litigation. Peck v. Commissioner, 90 T.C. 162, 166-67 (1988), aff'd, 904 F.2d 525 (9th Cir. 1990).

In its protest, [redacted] presents a strong case for the application of collateral estoppel (although it uses the broader, and somewhat misleading term, res judicata). We will briefly summarize [redacted] argument and then analyze its strengths and weaknesses. [redacted] first states the general proposition that res judicata and collateral estoppel apply to decisions by administrative agencies acting in their judicial capacities. United States v. Utah Construction & Mining Co, 384 U.S. 394, 422 (1966). Specifically, courts have applied res judicata and collateral estoppel to decisions by the RRB. Scammerhorn v. Railroad Retirement Board, 748 F.2d 1008, 1010 (5th Cir. 1984); Castillo v. Railroad Retirement Board, 725 F.2d 1012, 1014 (5th Cir. 1984). The protest then discusses Sunshine Anthracite Coal Co. v. Adkins, 310 U.S. 381 (1939), which is probably [redacted]'s most potent citation. The plaintiff in Sunshine Anthracite Coal applied for an exemption from the Bituminous Coal Conservation Act. However, the Bituminous Coal Commission handed down an opinion that the plaintiff's coal was bituminous, one of the potential consequences of which being the imposition of a federal excise tax on bituminous coal. The Service attempted to collect the excise tax and the taxpayer objected, asserting among other things that it was not bound by the Coal Commission's decision because the tax assessment was not at issue in the first proceeding. The Supreme Court determined that the company was precluded from litigating the excise tax liability. For one thing, the Court stated that there was privity between the Coal Commission and the Service. 310 U.S. at 402-03. The Court also concluded that the underlying issue in both cases was the same and that the Service was "merely the agency to collect taxes levied under the Act." Id. at 401-02. [redacted] then observed in its protest that the definition of "employer" is the same under both the RRA and the RRTA.

The strength of [redacted] argument is that it flows from the general rules of law arising from the above mentioned cases. Its argument also intuitively make sense: [redacted] was involved in a long, protracted dispute with the general counsel's office in one government agency and now, after successfully presenting its case before the RRB, must argue substantially the same issue again with another government agency unless collateral estoppel is applied. [redacted] argument would present tangible litigating hazards to the government if this case went to trial.

However, a closer examination detects several flaws in [redacted] case for collateral estoppel. First, the two cases giving preclusive effect to RRB decisions are of doubtful value in this case. Scammerhorn dealt with a widow who opted for one type of benefit and then subsequently applied for another type. Her claim was disallowed in 1977 by the RRB, and she failed to file an appeal to the U.S. Circuit Court of Appeals. After her second claim was disallowed in 1982, she appealed. The Fifth Circuit

held that res judicata applied. This case is distinguishable in that it is a private party, not the government, who is being precluded. Furthermore, the same cause of action is involved in Scammerhorn. 748 F.2d at 1010. In Castillo, another Fifth Circuit case, it was the RRB itself being estopped, but the case's precedential value is weakened by its misapplication of collateral estoppel. The plaintiff in Castillo applied for a disability annuity. The RRB decided that he had completed at least 120 months of applicable service (the first requirement), but was not disabled (the second requirement). Castillo later applied for a retirement annuity, but the RRB held that he did not have the required 120 months of service. On appeal, the Fifth Circuit correctly determined that there were two causes of action and that collateral estoppel was applicable. The court applied the doctrine, even though the finding as to the number of months of service was not an essential part of the first proceeding. 725 F.2d at 1013-14.

An analysis of the Sunshine Anthracite Coal case leads to a possible defense for the government to prevent the application of collateral estoppel in this case. In Sunshine Anthracite Coal, the excise tax was established originally in the Bituminous Coal Conservation Act itself, not in separate legislation. 310 U.S. at 389. This could be an important distinction because the government's response to [redacted] must be centered on the fact that two separate statutes, the RRA and the RRTA, are at issue and thus the issues are not identical. Although the results are mixed, some courts have declined to estop parties from litigating again if a different statute is involved. In Lane v. Railroad Retirement Board, the Sixth Circuit decided against applying collateral estoppel where the National Railroad Adjustment Board decided that a person was a railroad employee, concluding that the Adjustment Board was dealing with a statute separate from the RRA. Therefore, the RRB could make an independent evaluation. 185 F.2d 819 (6th Cir. 1950). The Sixth Circuit decided in a later case that collateral estoppel did not apply where the National Labor Relations Act was at issue in the first proceeding and the Civil Rights Act was at issue in the second because the two statutes were not sufficiently similar. Tipler v. E.I. DuPont deNemours and Co., 443 F.2d 125 (6th Cir. 1971).

A related argument is that there is no privity between the RRB and the Service. Although the general rule annunciated in Sunshine Anthracite Coal is that government agencies are in privity with each other, the Supreme Court carved out an exception in United States v. Radio Corporation of America, 358 U.S. 334 (1959). The Court decided that since the Federal Communications Commission did not have the power to decide antitrust questions, the Department of Justice could pursue an antitrust case in regard to a swap of television stations even though it had been approved by the Commission. The Court

implicitly determined that there was no privity between the Commission and the Justice Department because Sunshine Anthracite Coal only applied where the governmental agency in the first proceeding had the authority to determine the issue presented in the second proceeding. 358 U.S. at 352.

A final argument available to the government is that it, as a litigant, did not have a right of appeal from the RRB's decision. Under 45 U.S.C.§ 355(f), a claimant may appeal a RRB decision to a U.S. Circuit Court of Appeals, but, by implication, the government cannot. Although there are no firm rules on this subject and nothing directly on point, courts have been reluctant to apply collateral estoppel where a party, for whatever reason, could not appeal the first decision. For example, dictum in Block v. U.S. International Trade Commission states that collateral estoppel would not be applicable in a second proceeding because the Commission's decision was not final and thus not subject to appeal. 777 F.2d 1568 (Fed. Cir. 1985). In fact, the case cited for the proposition that res judicata applies to administrative decisions, Utah Construction, states that "an opportunity to seek court review of any adverse findings" is one of the factors that shows that an administrative agency is acting in a judicial capacity. 384 U.S. at 422.

All three arguments that the government can advance are dependent, at least to some extent, on the assumption that the RRA and the RRTA are separable in a meaningful way. (This is particularly true for the first argument, that the issues in the two proceedings are not identical.) However, the government's case is weakened in this respect by the Service's issuance of Rev. Rul. 74-121, 1974-1 C.B. 300. In that revenue ruling, the Service stated "The definitions of 'employer' under the Railroad Retirement Tax Act and the Railroad Retirement Act ... are the same." Such a position obviously undercuts any argument the government has that the two statutes should be treated separately.

In conclusion, the government can make a technical argument that collateral estoppel should not apply in this circumstance. However, as described above, there are litigation hazards involved should this case go to trial. These hazards are increased by the Service position in Rev. Rul. 74-121.

Issue 3:

CCDM (39)636.22 provides that the Assistant Chief Counsel (Employee Benefits and Exempt Organizations) is responsible for all coordination procedures between the Service and the RRB involving technical questions referred to the National Office. The procedures provide for exchanging views on interpretation of law, coverage status of persons involved, proposed decisions

contrary to the other agency's decisions, and proposed broad scope rulings. If a question is raised regarding a determination by the RRB under the RRA, the Service advises the RRB of its views by letter requesting the RRB's comments. Informal conferences may be held between the agencies in an effort to reach the same conclusion for tax and benefit purposes. If no agreement is reached, the Assistant Chief Counsel (Employee Benefits and Exempt Organizations) refers the matter by memorandum to the Associate Chief Counsel (Technical) showing the areas of disagreement and the coordination efforts.

Unlike the coordination procedures between the Service and the Social Security Administration where a Presidential directive requires the two agencies to join in submitting to the Attorney General for advice any case in which they have divergent coverage views (CCDM (39)636.1), there is no similar directive for the Service and the RRB. However, Executive Order 12146, Management of Federal Legal Resources, sections 1-401 and 402, generally provides that agencies submit disputes to the Attorney General, whenever agencies are unable to resolve a legal dispute between them. We believe this Executive Order, however, is more geared to situations where two agencies might sue one another in court. Since the institution of a refund suit would not cause the RRB to be a litigant against the Service, Executive Order 12146 would not be applicable for resolving the disagreement between the Service and the RRB regarding [redacted] coverage under the railroad retirement system.

In any event, on June 7, 1991, pursuant to CCDM (39)636.22, the Employee Benefits and Exempt Organization (EBEO) Division informally discussed with the RRB the conflicting views regarding [redacted] coverage status for tax and benefits purposes. The EBEO Division was advised that a prior RRB issued the conflicting decision and that the current RRB would be reluctant to reconsider that decision. EBEO was also advised that even if the current RRB reconsidered the matter, it would not be able to do so before the expiration of the statute of limitations on assessment. EBEO, nevertheless, advised us that it will begin formal coordination with the RRB with the hope that by the time [redacted] files its refund suit, the conflict will have been resolved.

Conclusion:

The Service is not bound by any decision rendered by the RRB because I.R.C. § 7801(a) vests the authority to administer and enforce the Internal Revenue Code solely with the Secretary of the Treasury. It is the Service's position that neither the doctrines of res judicata nor collateral estoppel apply. The procedure for resolving disputes between the two agencies is set forth in CCDM (39)636.22. EBEO will begin formal coordination

with the RRB so that, hopefully, by the time [redacted] files its refund suit, the conflict will have been resolved. If you should have any further questions, please call Will E. McLeod at FTS 566-3407.

MARLENE GROSS

By: _____
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